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Nos. 87-1584 and 87-1663

In the Supreme Court of the United States

OCTOBER TERM, 1987

GELDERMANN, INC., PETITIONER

v.

COMMODITY FUTURES TRADING COMMISSION

BOARD OF TRADE OF CITY OF CHICAGO, PETITIONER

v.

COMMODITY FUTURES TRADING COMMISSION

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether the Commodity Futures Trading Commission exceeded its statutory authority or acted arbitrarily in adopting a rule requiring the members of the Board of Trade of the City of Chicago to arbitrate customers' claims at the customers' option.

2. Whether Section 5a(11) of the Commodity Exchange Act, 7 U.S.C. 7a(11), which requires regulated futures contract markets to provide customers of members the option of pursuing fair and equitable procedures for the arbitration of claims against a member, violates Article III of the Constitution or the Seventh Amendment.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	7
Conclusion	15

TABLE OF AUTHORITIES

Cases:

Atlas Roofing Co. v. *OSHRC*, 430 U.S. 442 (1977) ... 6
Block v. *Hirsh*, 256 U.S. 135 (1921) ... 14
Board of Trade v. *CFTC*, 704 F.2d 929 (7th Cir. 1983) 4
Board of Trade v. *Olsen*, 262 U.S. 1 (1923) ... 10
CFTC v. *Schor*, No. 85-621 (July 7, 1986) ... 3, 5, 6, 10, 13, 14
Chevron U.S.A. Inc. v. *NRDC, Inc.*, 467 U.S. 837 (1984) 7
Dean Witter Reynolds Inc. v. *Byrd*, 470 U.S. 213 (1985) 12
McDonald v. *City of West Branch*, 466 U.S. 284 (1984) 13
Moses H. Cone Memorial Hosp. v. *Mercury Constr. Corp.*, 460 U.S. 1 (1983) ... 12
Nelson v. *Secretary of Agriculture*, 133 F.2d 453 (7th Cir. 1942) ... 11
NLRB v. *Jones & Laughlin Steel Corp.*, 301 U.S. 1 (1937) 6
Northern Pipeline Co. v. *Marathon Pipe Line Co.*, 458 U.S. 50 (1982) ... 13
Pernell v. *Southall Realty*, 416 U.S. 363 (1974) ... 14
Prima Paint Corp. v. *Flood & Conklin Mfg.*, 388 U.S. 395 (1967) ... 9
Shearson/American Express, Inc. v. *McMahon*, No. 86-44 (June 8, 1987) ... 12
Thomas v. *Union Carbide Agricultural Prods. Co.*, 473 U.S. 568 (1985) ... 5, 9, 10, 13
Tull v. *United States*, No. 85-1259 (Apr. 28, 1987) ... 14

Constitution, statutes and regulation:

U.S. Const.:
Art. I ... 10
Art. III ... *passim*

Constitution, statutes and regulation—Continued: Page

§ 1 5
Amend. V (Due Process Clause) 9
Amend. VII 3, 5, 6, 14
Administrative Procedure Act, 5 U.S.C. (& Supp. IV) 701 *et seq.* 4
Arbitration Act, 9 U.S.C. 1 *et seq.* 12
Commodity Exchange Act, 7 U.S.C. (& Supp. IV) 1 *et seq.* 2
§ 2(a)(1)(A), 7 U.S.C. 2 ..... 2, 12
§ 3, 7 U.S.C. 5 2
§ 4(a), 7 U.S.C. 6(a) 2
§ 4(a), 7 U.S.C. 6(a)(2) 11
§ 4d(1), 7 U.S.C. 6d(1) 12
§ 5, 7 U.S.C. 7 2
§ 5a(11), 7 U.S.C. 7a(11) 2, 3, 4, 5, 6, 7, 8, 12
§ 6(a), 7 U.S.C. 8 2
§ 6(b), 7 U.S.C. 9 2
§ 8a(7), 7 U.S.C. 12a(7) 3
§ 14, 7 U.S.C. 18 2
Federal Insecticide, Fungicide and Rodenticide Act, 7 U.S.C. (& Supp. IV) 136 *et seq.* 9
Futures Trading Act of 1982, Pub. L. No. 97-444, § 217(a), 96 Stat. 2307 8
28 U.S.C. 1441(b) 9
17 C.F.R. 7.201 ..... 3, 5, 7, 8

Miscellaneous:

Commodity Futures Trading Commission Act: Hearings on S. 2485, S. 2578, S. 2837, and H.R. 13113 Before the Senate Comm. on Agriculture and Forestry, 93d Cong., 2d Sess. (1974) 8
41 Fed. Reg. 27526 (1976) 8
H.R. Rep. 97-565, 97th Cong., 2d Sess. Pt. 1 (1982) .. 8

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OPINIONS BELOW

The opinion of the court of appeals (87-1584 Pet. App. 1-26) is reported at 836 F.2d 310. The opinion of the district court (87-1584 Pet. App. 27-38) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on December 22, 1987. The petitions for a writ of certiorari were filed on March 21, 1988. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. The Commodity Exchange Act, 7 U.S.C. (& Supp. IV) 1 *et seq.* (CEA or Act), governs trading in futures contracts on "boards of trade," which are "exchange[s] or association[s] * * * engaged in the business of buying or selling any commodity or receiving the same for sale on consignment" (7 U.S.C. 2). The Act declares that transactions in commodity futures contracts "are affected with a national public interest" (7 U.S.C. 5). Accordingly, the Act gives the Commodity Futures Trading Commission (CFTC or Commission) the power to designate as "contract markets" boards of trade that satisfy certain requirements, and provides generally that commodity futures transactions in the United States may be executed lawfully only on contract markets and only through members of those markets. See 7 U.S.C. 6(a), 7, 8. The Commission oversees the operation of contract markets and has the authority to bring an administrative proceeding to suspend "all trading privileges" of, and otherwise sanction, any person who violates the Act or the Commission's regulations (7 U.S.C. 9).

The Act imposes certain duties on designated contract markets and their members. One of a contract market's duties, imposed by Section 5a(11) of the Act (7 U.S.C. 7a(11) (emphasis in original)), is to:

> [p]rovide a fair and equitable procedure through arbitration or otherwise * * * for the settlement of customers' claims and grievances against any member or employee thereof: *Provided,* That (i) the use of such procedure by a customer shall be voluntary and (ii) the term "customer" as used in this paragraph shall not include another member of the contract market * * *.[1]

[1] The Act also provides a reparations procedure through which customers of commodity brokers may seek redress for the brokers' violations of the Act or the Commission's rules. See 7 U.S.C. 18. The

After Section 5a(11) was enacted, all 11 exchanges designated as contract markets submitted to the Commission for its approval proposed rules providing for arbitration of customers' claims against their members. Alone among the 11, petitioner Board of Trade of the City of Chicago (Board of Trade) submitted a proposed rule that did not give customers an absolute right to have their claims arbitrated; instead, the rule gave members of the Board of Trade the choice whether to agree to arbitration. The Board of Trade was thus the only futures market of the 11 markets then in existence not to adopt a rule requiring members to arbitrate claims by their customers. 87-1584 Pet. App. 4.

Under Section 8a(7) of the Act (7 U.S.C. 12a(7)), the CFTC is authorized "to alter or supplement the rules of a contract market * * * for the protection of traders or to insure fair dealings * * *." The CFTC asked the Board of Trade to amend its rule to require that its members submit customer claims to arbitration when the customer requests it. The Commission explained that such an amendment was required by Section 5a(11) of the Act—*i.e.*, that the section was intended to give the option to seek arbitration to the customer, not to the member of a contract market. The Board of Trade, however, refused to amend its proposed rule. Therefore, the CFTC, acting pursuant to Section 8a(7) of the Act, adopted Rule 7.201 (17 C.F.R. 7.201), which requires members of the Board of Trade to enter into arbitration of their customers' claims when the customer invokes arbitration. 87-1584 Pet. App. 5.[2]

Commission is assigned the task of administering this procedure, which was described by this Court in *CFTC* v. *Schor*, No. 85-621 (July 7, 1986), slip op. 2, as an "alternative to existing fora available to aggrieved customers, namely, the courts and arbitration."

[2] The Board of Trade immediately sought judicial review of Rule 7.201 on the ground that it deprived members of the Board of Trade of their Seventh Amendment right to a jury trial. The Seventh Circuit

2. Petitioner Geldermann, Inc., a commodity brokerage firm, is registered with the CFTC and is a member of the Board of Trade. In April 1985, FSI Futures, Inc. (FSI) initiated an arbitration proceeding against Geldermann. FSI claimed that Geldermann did not properly fill one of FSI's orders. Geldermann did not contest FSI's right to arbitration, and a Board of Trade arbitration panel awarded $54,718 to FSI. Soon thereafter, Geldermann notified FSI that it was terminating FSI's account. 87-1584 Pet. App. 19.

In May 1985, FSI again sought to arbitrate claims against Geldermann. FSI asserted claims for losses suffered in transferring its positions from Geldermann, and for interest allegedly due as a result of Geldermann's late payment of the first arbitration award. This time, Geldermann opposed FSI's arbitration demand. To avoid penalties for noncompliance with the rule requiring members to arbitrate customers' claims, Geldermann filed this action for an injunction against the CFTC and the Board of Trade. 87-1584 Pet. App. 19.[3]

3. The district court granted Geldermann's motion for summary judgment and permanently enjoined the CFTC from requiring Geldermann to arbitrate FSI's claims (87-1584 Pet. App. 39). The court held that the Commis-

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dismissed that action as not ripe. See *Board of Trade* v. *CFTC*, 704 F.2d 929 (1983). The court noted that the validity of the CFTC's rule could be tested by a member bringing suit to enjoin an arbitration proceeding demanded by a customer. See *id.* at 933. The Board of Trade published this dictum in a footnote to its rules. See 87-1584 Pet. App. 2-3.

[3] Geldermann's action against the Commission was brought under the Administrative Procedure Act (5 U.S.C. (& Supp. IV) 701 *et seq.*). Although the Board of Trade was named as a defendant, the Board of Trade supported Geldermann's position. In the court of appeals, therefore, the Board of Trade was aligned with Geldermann as an appellee (87-1584 Pet. App. 1).

sion's rule requiring members of the Board of Trade to submit to arbitration (17 C.F.R. 7.201) violated Geldermann's Seventh Amendment right to a trial by jury (87-1584 Pet. App. 33).[4] The district court further held that Geldermann had not waived its Seventh Amendment rights even though Geldermann, in becoming a member of the Board of Trade, agreed to abide by the Board of Trade's rules (*id.* at 35).

The court of appeals reversed. The court first ruled that the CFTC had reasonably concluded that Section 5a(11) of the Act compels designated contract markets to have rules requiring members to arbitrate claims at a customer's request (87-1584 Pet. App. 10-11). The court of appeals then rejected Geldermann's Article III challenge to Section 5a(11). The court, citing this Court's decision in *CFTC* v. *Schor,* No. 85-621 (July 7, 1986), considered the two main purposes served by Section 1 of Article III: to safeguard a litigant's personal right to have claims decided by judges with life tenure and other protections, and to protect the role of the judiciary within our constitutional scheme of tripartite government (87-1584 Pet. App. 11-25).

The court of appeals cited this Court's decisions in *Thomas* v. *Union Carbide Agricultural Prods. Co.*, 473 U.S. 568 (1985), and *CFTC* v. *Schor, supra,* and held that Geldermann had waived any personal right it might have had to an Article III forum (87-1584 Pet. App. 21). The court noted that Geldermann signed an agreement to abide by the Board of Trade's regulations; one of those regulations is the requirement that members must arbitrate claims at a customer's request (*id.* at 15). The court of appeals rejected Geldermann's claim that its consent was not voluntary.

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[4] The district court ruled that Commission Rule 7.201 was not mandated by Section 5a(11) of the Commodity Exchange Act. Thus the court considered the constitutionality of Rule 7.201, not Section 5a(11) (87-1584 Pet. App. 32).

The court observed that Geldermann was not compelled to become a member of the Board of Trade, and that Geldermann could preserve any right to an Article III court "by resigning its membership" (*id.* at 18 n.9.). The court also noted that Geldermann willingly consented to the first arbitration with FSI, which showed that Geldermann was "content to have [its] disputes settled by a non-Article III forum until [it] lost" (*id.* at 21).[5]

The court of appeals next ruled that Section 5a(11) of the Act does not exceed the non-waivable structural limits that Article III places on Congress (87-1584 Pet. App. 21-25). The court reached this conclusion by comparing this case to *CFTC* v. *Schor, supra,* in which the Court rejected an Article III challenge to the adjudication of common law counterclaims in connection with the reparation procedures under the CEA. The court of appeals stated that this Court would likely view the congressional scheme of allowing commodity futures customers the option of electing arbitration "as intruding on the province of the judiciary even less than the reparations procedure challenged in *Schor*" (87-1584 Pet. App. 23).

Finally, the court of appeals rejected Geldermann's contention that it has a Seventh Amendment right to a jury trial on FSI's claims (87-1584 Pet. App. 26). Citing *Atlas Roofing Co.* v. *OSHRC,* 430 U.S. 442, 449-461 (1977), and *NLRB* v. *Jones & Laughlin Steel Corp.,* 301 U.S. 1, 48-49 (1937), the court of appeals stated that the Seventh Amendment "simply does not apply" in a non-Article III forum (87-1584 Pet. App. 26). Because Geldermann was not en-

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[5] In this respect, the court of appeals compared Geldermann to the respondent in *CFTC* v. *Schor, supra,* who objected to adjudication of common law claims in an administrative proceeding under the CEA only after adjudication of those claims: "Schor and Geldermann were content to have their disputes settled by a non-Article III forum until they lost" (87-1584 Pet. App. 21).

titled to an Article III forum, the court concluded that "the Seventh Amendment is not implicated" in this case (*ibid.*).

ARGUMENT

The court of appeals' decision is correct and does not conflict with any decision of this Court or any other court of appeals. No further review is warranted.

1. The Board of Trade argues (87-1663 Pet. 10-14) that the Commission exceeded its authority or acted arbitrarily in adopting Rule 7.201, which requires members of the Board of Trade to enter into arbitration of a customer's claim whenever the customer chooses that forum. The Commission's rule, however, is in full accord with the language and purpose of the relevant provision of the CEA.[6]

Section 5a(11) of the CEA states that "[e]ach contract market *shall* * * * [p]rovide a fair and equitable procedure through arbitration or otherwise * * * for the settlement of customers' claims and grievances against any member or employee thereof: *Provided,* That (i) the use of such procedure by a customer shall be voluntary * * * " (7 U.S.C. 7a(11) (emphasis added)). The purpose evident in this language is to give customers of a member of a contract market the right, at their option, of arbitrating claims against the member. For that congressionally mandated option to be meaningful, members of a contract market must be required to submit to arbitration of claims at a customer's request.[7]

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[6] Of course, under *Chevron U.S.A. Inc.* v. *NRDC, Inc.*, 467 U.S. 837, 845 (1984), unless the text of the statute and its legislative history conclusively resolve the question of interpretation *against* the Commission, the Commission's consistent interpretation of the CEA must be upheld if it is "a reasonable one."

[7] The statute (7 U.S.C. 7a(11)) requires the contract market to provide a fair procedure "through arbitration or otherwise." No one has

The legislative and administrative history of the provision is wholly consistent with this interpretation. When the Senate was considering in 1974 the bill that contained Section 5a(11), two representatives of the Board of Trade objected to the bill on the ground that it gave the customer, but not the member of a contract market, the option to avoid arbitration. *Commodity Futures Trading Commission Act: Hearings on S. 2485, S. 2578, S. 2837, and H.R. 13113 Before the Senate Comm. on Agriculture and Forestry,* 93d Cong., 2d Sess. 524, 526 (1974). Congress passed the law over those objections. The Commission has consistently interpreted Section 5a(11) to give the customer the right to choose arbitration. See 41 Fed. Reg. 27526 (1976). In 1983, Congress amended Section 5a(11) in the Futures Trading Act of 1982, Pub. L. No. 97-444, § 217(a), 96 Stat. 2307. The House Committee Report noted at that time that the amendment did "not affect the existing requirement that the use of arbitration by the customer is voluntary or the Commission's understanding that exchange members must participate in arbitration proceedings which the customer has elected to pursue" (H.R. Rep. 97-565, 97th Cong., 2d Sess. Pt. 1, at 56 (1982)). It is clear, therefore, that the Commission did not exceed its statutory authority or act arbitrarily in adopting Rule 7.201.

2. Petitioners' principal contention (87-1584 Pet. 18-19; 87-1663 Pet. 14-19) is that Section 5a(11) of the CEA is unconstitutional because it deprives members of contract markets of a supposed "personal right" to have customers' claims against them adjudicated in an Article III forum.

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suggested that the words "or otherwise" alter the issue in this case. Whatever latitude those words may allow for a fair procedure that involves processes other than arbitration, they do not allow the market to select arbitration as the "fair and equitable procedure" and then make members' participation voluntary, as the Board of Trade attempted here.

But the claim as articulated by petitioners is plainly wrong; they have neither a statutory nor a constitutional right to be proceeded against in an Article III court. Petitioners stress (87-1584 Pet. 11-12; 87-1663 Pet. 20), that FSI's claims are essentially state common law claims sounding in "contract, debt and conversion" (87-1584 Pet. App. 33). Geldermann clearly has no *constitutional* right to have such claims adjudicated in a federal court. Indeed, because Geldermann is an Illinois citizen (*id.* at 22 n.11), if FSI had asserted state-law claims in an Illinois court, Geldermann could not have removed the action to a federal court even though there apparently is diversity of citizenship. See 28 U.S.C. 1441(b).

Petitioners' real contention, not articulated below or in the petitions, is that members of regulated futures markets have a constitutional right (perhaps grounded in the Due Process Clause) to insist that customers' claims against them be resolved by some judicial process and to refuse to resolve them through arbitration. That claim is wrong. The arbitration process itself, conducted under rules adopted by a board of trade, is obviously not inherently unfair to members. Cf. *Prima Paint Corp.* v. *Flood & Conklin Mfg.*, 388 U.S. 395 (1967) (upholding constitutionality of the federal Arbitration Act). And Congress may constitutionally require boards of trade to afford arbitration if it deems that appropriate to protect customers by providing an efficient remedy for their claims.

In *Thomas* v. *Union Carbide Agricultural Prods. Co.*, *supra*, the Court considered the constitutionality of the arbitration requirements of the Federal Insecticide, Fungicide, and Rodenticide Act (7 U.S.C. (& Supp. IV) 136 *et seq.* (FIFRA)). Under that statute, a manufacturer must register its pesticides with the Environmental Protection Agency. To obtain a registration, the manufacturer must submit a large amount of data to the agency. As part of the process,

the submitting manufacturer agrees that subsequent registrants may rely on its data when they register their pesticides, and it agrees to accept compensation for this use as determined (in the absence of an agreement) by arbitration. Follow-on registrants, in turn, agree to pay compensation, determined by an arbitrator, for using an earlier registrant's data. Hence, consent to arbitration is a condition to registering a pesticide for sale and to gaining the benefits of an earlier registrant's data. In upholding this scheme, the Court noted that Congress has the power under Article I of the Constitution "*to condition* issuance of registrations or licenses on compliance with agency [arbitration] procedures" (473 U.S. at 589 (emphasis added)), and that "the follow-on registrant * * * explicitly consents to have his rights determined by arbitration" (*id.* at 592). See also *Schor,* slip op. 15-16 (one who seeks relief in a CFTC reparations proceeding validly waives, in return for the benefits of that procedure, the right to insist that a common law counterclaim be brought in an Article III court).

A member's consent to the arbitration of customer claims is likewise a reasonable condition of membership in a regulated futures market. Some 65 years ago the Court noted that the "Board of Trade conducts a business which is affected with a public interest and is, therefore, subject to reasonable regulation in the public interest." *Board of Trade* v. *Olsen,* 262 U.S. 1, 40-41 (1923). Congress has conferred a very special status on members of the Board of Trade and other regulated contract markets: the Act requires (see page 2, *supra*) that all trading in futures contracts be conducted through members of such markets. Congress imposed that requirement in order to permit "careful supervision of those transactions in the national public interest" (*Olsen*, 262 U.S. at 41). Accordingly, under the CEA, anyone who wishes to trade in commodity futures contracts must have its trades "executed or consummated by or

through a member of [a] contract market" (7 U.S.C. 6(a)(2)). Having th s placed members in the neck of the bottle, Congress could surely provide that members must, through their self-regulatory organizations, provide a just and efficient means of resolving customer claims. See generally *Nelson* v. *Secretary of Agriculture,* 133 F.2d 453, 456 (7th Cir. 1943) (member firm is permitted "to engage in a business affected with the national public interest in which * * * [it] may participate only upon compliance with conditions imposed by Congress in the exercise of its power over commerce").

Geldermann chose to have the economic and other benefits of being a member of a federally regulated futures contract market.[8] Those benefits flow, in part, from government regulation itself, which gives investors confidence in the integrity of contract markets, the honesty of their members, and (not incidentally) the availability of remedies for the misconduct of members.[9] Such membership is not essential to engage in the business of trading in futures contracts; indeed, FSI is a "futures commission merchant" under the Commodity Exchange Act[10] but not a member of the

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[8] That choice, and Geldermann's agreement to be bound by the Board of Trade's arbitration rule (87-1584 Pet. App. 15), led the court of appeals to conclude that Geldermann "waived" any personal right to an Article III forum. The court meant, as we read its opinion, only that Congress may provide that those who choose to be members of a regulated futures market must agree to an efficient and fair procedure for resolution of customer claims.

[9] Geldermann's president noted that membership in a regulated market is "reassuring to significant commercial customer entities" (87-1584 Pet. App. 45).

[10] A "futures commission merchant" is any person that solicits or accepts "orders for the purchase or sale of any commodity for future delivery on or subject to the rules of any contract market and that, in or in connection with such solicitation or acceptance of orders, accepts any money, securities, or property * * * to margin, guarantee,

Board of Trade (87-1584 Pet. App. 29). But Congress has determined that those firms, like Geldermann, that seek and obtain membership in a designated contract market, and thus join the select group through which others must deal, should agree to submit to fair and equitable arbitration of customers' claims in order to permit their efficient resolution.[11] That congressional determination has the same rational and constitutional bases as the determination that those who choose to participate in the FIFRA registration process (*Thomas*) or those who seek reparations from the CFTC (*Schor*) must thereby agree to non-Article III resolution of certain claims against them. Cf. *Shearson/American Express Inc.* v. *McMahon,* No. 86-44 (June 8, 1987), slip op. 17 (enforcing agreement to arbitrate claims under the Securities Exchange Act in light of SEC's "statutory authority to ensure that arbitration is adequate to vindicate Exchange Act rights").

3. Petitioners also argue that Section 5a(11) and the Commission's arbitration rule violate the "structural" principle of Article III (87-1584 Pet. 19; 87-1663 Pet. 22-25),

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or secure any trades or contracts that result or may result therefrom" (7 U.S.C. 2). It is unlawful for any person to act as a futures commission merchant unless he is registered as such with the Commission. See 7 U.S.C. 6d(1).

[11] This Court has consistently respected Congress's decisions to encourage or compel arbitration of claims. In *Moses H. Cone Memorial Hosp.* v. *Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983), the Court said that the Arbitration Act (9 U.S.C. 1 *et seq.*) manifests a "liberal policy favoring arbitration agreements." This "policy requires that [the Court] rigorously enforce agreements to arbitrate." *Dean Witter Reynolds Inc.* v. *Byrd,* 470 U.S. 213, 221 (1985). Indeed, "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability" (*Moses H. Cone Memorial Hosp.*, 460 U.S. at 24-25 (footnote omitted)).

but they fundamentally misunderstand that principle. In *Schor,* the Court articulated it as follows: "Article III, § 1 safeguards the role of the Judicial Branch in our tripartite system by barring congressional attempts '*to transfer jurisdiction to non-Article III tribunals* for the purpose of emasculating' constitutional courts, and thereby preventing 'the encroachment or aggrandizement of one branch at the expense of the other' " (*Schor*, slip op. 16 (citations omitted; emphasis added)). Later in *Schor,* the Court said that Congress risks violating this principle when it "encroache[s] on the federal judiciary" by allocating matters traditionally tried before an Article III court "*to a non-Article III forum of its own creation*" (*id.* at 20 (emphasis added)).[12]

This case involves no transfer of any part of the judicial power to a non-Article III federal forum. Arbitration under procedures established by the Board of Trade is an essentially private dispute resolution mechanism. Arbitrators are privately appointed; under the Board of Trade's rules, the customer has the option of selecting a panel composed of persons associated with the Board of Trade (*e.g.*, traders and brokers) or a panel with a majority of members who are not connected with the Board of Trade. In either case, the arbitrators are not officers of any branch of the federal government, and they do not exercise government power. Their function is not to adjudicate but to resolve disputes without adjudication. Cf. *McDonald* v. *City of West Branch,* 466 U.S. 284, 291 (1984) ("arbitral factfinding is generally not equivalent to judicial factfinding"). In sum, Congress has not "encroached on the federal judiciary" by transferring part of the judicial power "to a non-Article III

[12] In *Thomas,* the Court described *Northern Pipeline Co.* v. *Marathon Pipe Line Co.*, 458 U.S. 50 (1982), as holding "only that Congress may not *vest in a non-Article III court the power to adjudicate*" certain kinds of claims without the consent of the litigants (473 U.S. at 584 (emphasis added)).

forum of its own creation" (*Schor,* slip op. 20); Congress has merely required that members of futures markets agree to afford an essentially private dispute resolution mechanism for customer claims arising out of transactions regulated under the CEA. Since members may constitutionally be required to resolve customer claims in that manner (see pages 8-12, *supra*), the Article III courts have not been deprived of anything that is rightfully theirs.[13]

4. Geldermann also argues (87-1584 Pet. 10-17) that it has a Seventh Amendment right to a jury trial on FSI's claims. As the court of appeals recognized (87-1584 Pet. App. 26), however, this argument is foreclosed by the fact that FSI validly invoked its statutory right to select a non-Article III forum.

In *Tull* v. *United States,* No. 85-1259 (Apr. 28, 1987), slip op. 5 n.4, this Court recently noted that "the Seventh Amendment is not applicable to administrative proceedings" because of "the practical limitations of a jury trial" and a jury trial's incompatibility "with proceedings outside of traditional courts of law." This comment in *Tull* was essentially a restatement of the holding of *Block* v. *Hirsh,* 256 U.S. 135 (1921), which "stands for the principle that the Seventh Amendment is generally inapplicable in administrative proceedings, where jury trials would be incompatible with the whole concept of administrative adjudication." *Pernell* v. *Southall Realty,* 416 U.S. 363, 383 (1974).

Arbitration, of course, is equally incompatible with jury trials. The very purpose of arbitration is to provide an efficent decision-making process without the complex procedures attendant to traditional court litigation. Accordingly, it follows from the fact that Congress may give

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[13] Congress has not, of course, attempted to "withdraw from judicial cognizance" (*Schor,* slip op. 20) the entire subject matter of customer claims; it has simply given the customer the option of invoking arbitration.

customers of members of contract markets the option of asserting claims against those members in arbitration, that the Constitution does not guarantee members a right to a jury trial on such claims. The cases cited by petitioners (87-1584 Pet. 11; 87-1663 Pet. 20) do not hold otherwise. They simply stand for the proposition that Geldermann might have had a right to a jury trial had FSI brought its claims in a federal court.

CONCLUSION

The petitions for a writ of certiorari should be denied.

Respectfully submitted.

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